

Mid-Cycle Budget Update

Fiscal Years 2016 & 2017



*East Bay Municipal Utility District
Oakland, California*

May 2016

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FY16 & FY17 MID-CYCLE BUDGET UPDATE

EXECUTIVE SUMMARY

The Board of Directors adopted the Fiscal Years 2016 & 2017 biennial budget on June 9, 2015 which allows the District to provide the highest quality water and wastewater services for our customers while maintaining fair and reasonable rates. This mid-cycle budget update reflects the status of the FY16 & FY17 budgets and projected changes to revenues, expenditures and staffing for the Water and Wastewater Systems.

Overview

The adopted budget for Fiscal Years 2016 & 2017 is \$1.83 billion. Of that amount, \$1.71 billion is for water system and wastewater system operations, debt service and capital appropriations. The remaining \$126.3 million represents drought contingency.

This budget focuses on three key strategic plan priorities – making sustained reinvestments in aging physical infrastructure, investing in critical information technology infrastructure, and managing the impacts of an extended drought. In FY16, significant progress has been made in each of these priority areas in addition to managing the ongoing challenges associated with a high level of retirements.

Drought Response and Water Supply

The past four years have been the driest in the history of the District. In April 2015, the Board took a number of actions to preserve the water supply through the declaration of a Stage 4 drought, authorization for the acquisition of supplemental water supplies conveyed through the Freeport Regional Water Facility and implementation of District-wide mandatory water use reductions.

Customers responded to the call to conserve. Overall customer demand reduction is at 24 percent since 2013, exceeding the District's goal of 20 percent, and the state requirement of 16 percent. This reduced demand has resulted in March 2016 water production being the lowest March water production since the District database which extends to 1961. As demonstrated by previous droughts, strong customer conservation levels are likely to continue for many years.

The water supply outlook has greatly improved as year-to-date precipitation has been above average. The projected September 30, 2016 total system storage is 630 thousand acre feet, resulting in the District's water supply being sufficient to meet customer demands. Looking ahead to FY17, recent direction from Governor Brown and the State Water Resources Control Board allows water suppliers to set their own conservation targets. The Board of Directors will consider which restrictions put in place during this drought should become permanent restrictions in the service area. The District remains committed to doing its part to maximize conservation in our system and assisting customers to be smart about water use.

Appropriations

The FY17 appropriations for both the Water and Wastewater Systems are shown below. The appropriations have been reviewed and no changes are recommended.

Based on the water supply projections, it is anticipated that no new drought-related expenses would be incurred in FY17 except any payments to finalize FY16 drought-related expenditures which are estimated to be less than \$5 million.

FY17 APPROPRIATIONS			
(\$ Thousands)			
	Water	Wastewater	Total
Operations	262,232	70,717	332,949
Debt Service	180,191	33,956	214,147
Capital Appropriation	<u>290,392</u>	<u>32,583</u>	<u>322,975</u>
Total	732,815	137,256	870,071
Drought Contingency	<u>62,078</u>	-	<u>62,078</u>
Grand Total	794,893	137,256	932,149

Staffing

The adopted FY16 & FY17 budget authorized the addition of three positions in the Water System in FY17. A change is proposed to add one temporary construction (TC) Construction Inspector position in the Water System to support a developer-funded pipeline project. Therefore, no additional funding is needed for this position.

There are no FY17 staffing changes for the Wastewater System.

Rates

No change is recommended to the adopted FY17 rate increase of 7.0 percent for the Water System or 5.0 percent increase for the Wastewater System. Since revenue shortfall from FY16 customer conservation is anticipated to continue in FY17, rate stabilization funds and budget savings are projected to be sufficient to balance the budget and meet District financial metrics. The FY17 Water System revenue projection considers the suspension of the drought surcharge.

Operating Budget Performance

Shown below are the projected net budget variances for both the water and wastewater systems.

Water System

Fiscal Year 2016

Significant customer conservation has impacted water sales. The FY16 revenue budget was based on average water sales of 151 million gallons per day (MGD). However, water sales for FY16 are expected to average 129 MGD resulting in water charges revenue of \$51 million less

than budgeted. Drought-related expenditures such as the purchase, treatment and delivery of supplemental water supplies created additional fiscal pressure. The subsequent shortfall is partially offset by revenue from the drought surcharge, increased SCC revenues and normal operations expense savings. Despite these offsets, the Water System is expected to end FY16 with an unfavorable net budget variance of \$3.5 million which will be offset by a drawdown of cash reserves. A projected \$11.6 million in rate stabilization funds will be used to maintain the District's policy level for debt coverage of 1.6.

Fiscal Year 2017

With an improved FY17 water supply projection, no supplemental water supplies should be necessary. Similar to FY16, the fiscal impact of decreased water consumption is anticipated to continue. The FY17 revenue budget, like FY16, was established on average water sales of 151 MGD. Based on historical patterns of continued customer conservation following a drought, average water sales for FY17 are anticipated to remain at 129 MGD, in line with the prior fiscal year. This will result in projected water charges revenue of \$55 million less than budgeted. While projected operating expense savings have been identified, they are insufficient to fully cover the anticipated revenue loss. Therefore, the Water System is projected to end FY17 with an unfavorable net budget variance of \$29.1 million. Rate stabilization funds will be utilized to maintain the District's policy level for debt coverage.

No new drought-related revenues or expenses are projected for FY17 with the exception of potential payments to finalize FY16 drought-related expenditures which are estimated to be less than \$5 million.

Wastewater System

Fiscal Year 2016

Wastewater revenues are much less sensitive to water demand levels than water charges revenue. Therefore, the Wastewater System is projected to end FY16 with a favorable net budget variance of \$6.3 million. Treatment charges are projected to be less than budget as a result of the customer conservation, but are more than offset by increased revenues from Resource Recovery, Capacity Charges and operating expense savings.

Fiscal Year 2017

Overall, FY17 is expected to end with a favorable net budget variance of \$3.2 million. Similar to FY16, treatment charges are projected to be less than budget as a result of continued customer conservation, but are more than offset by increased revenues from Resource Recovery and operating expense savings.

Capital Budget Performance

Water System

Water System FY16 capital cash flow expenditures are projected to total \$207.0 million or 93 percent of the planned cash flow of \$224.5 million. For FY17, the Water System capital cash flow expenditures are projected to fall within the total appropriation approved by the Board.

Wastewater System

Wastewater System FY16 capital cash flow expenditures are projected to total \$36.4 million or 94 percent of the planned cash flow of \$39.0 million. For FY17, the Wastewater System capital cash flow expenditures are projected to fall within the total appropriation approved by the Board.

WATER SYSTEM

Fiscal Year 2016

Summary

Customer conservation has exceeded expectations causing a significant decrease in water consumption. While projected net revenues of \$11.3 million are greater than budget primarily as a result of drought surcharge revenues, total operating expenses were \$14.8 million greater than budget due to drought-related costs. The Water System is projected to end FY16 with an unfavorable net budget variance of \$3.5 million which will be offset by a drawdown of cash reserves. Approximately \$11.6 million in rate stabilization funds will be used to maintain the District's policy level for debt coverage.

The following table presents the FY16 Water System revenue and operating expense projection compared to budget, followed by a description of the key budget drivers.

FY16 Water System Revenue and Expenses (\$Millions)	Amended Budget	Year-end Projection	Variance Favorable / (Unfavorable)	% of Budget
Operating Revenues:				
Water Charges	422.8	371.8	(51.0)	88%
Property Taxes	24.5	24.5	-	100%
Power Sales	3.5	3.5	-	100%
Interest Income	1.7	1.7	-	100%
SCC Revenues	24.6	35.0	10.4	142%
Reimbursements	10.9	10.9	-	100%
All Other Revenue	17.2	17.2	-	100%
Drought Surcharge / Excessive Use		51.9	51.9	
TOTAL REVENUES	505.2	516.5	11.3	102%
Operating Expenses:				
Operations	248.3	239.8	8.5	97%
Debt Service	169.9	167.3	2.6	98%
Drought Expenses ¹		25.9	(25.9)	N/A
TOTAL OPERATING EXPENSES	418.2	433.0	(14.8)	104%

NET VARIANCE COMPARED TO BUDGET	(3.5)	-
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¹ Drought contingency appropriation of \$64.2 million not shown above.

Revenues

Total revenues are projected to be \$516.5 million or 102 percent of budget. Water charges are projected to be \$51.0 million less than budget due to customer conservation during the drought.

The budget assumed an average of 151 MGD whereas year-end water sales projections are estimated to average 129 MGD. The water charges revenue shortfall is mitigated by a projected \$51.9 million in Stage 4 drought surcharge revenues, and SCC revenues which are projected \$10.4 million greater than budget due to increased building activity within the service area.

Expenses

Total operating expenses are projected to be \$14.8 million greater than budget due to drought-related expenditures. Normal non drought operations costs are projected to be \$11.1 million less than budget primarily due to unspent contingency, higher than budgeted operating reimbursements for the administration of capital projects, slightly lower debt service expenses, and other operation expense savings. Drought-related expenses are estimated to be \$25.9 million which is lower than anticipated since water year 2016 supplemental water supply purchases are not necessary given the projected water supply.

Net Budget Variance

Despite the above revenue and normal operations expense saving offsets, the Water System is projected to end FY16 with an unfavorable net budget variance of \$3.5 million which will be offset by a drawdown of cash reserves. Rate stabilization funds will be used to maintain the District's policy level for debt coverage of 1.6.

Fiscal Year 2017

Summary

Based on historical patterns of continued customer conservation following a drought, average water sales for FY17 are anticipated to remain at 129 MGD, in line with the prior fiscal year. This will result in water charges revenue totaling \$55 million less than budgeted. This projected revenue loss is partially offset by operating expense savings, but is expected to result in an unfavorable net budget variance of \$29.1 million. Rate stabilization funds will be utilized to maintain the District's policy level for debt coverage.

The following table presents the FY17 Water System revenue and operating expense projection compared to budget, followed by a description of the key budget drivers.

FY17 Water System Revenue and Expenses (\$Millions)	Adopted Budget	Year-end Projection	Variance Favorable / (Unfavorable)	% of Budget
Operating Revenues:				
Water Charges	453.0	398.0	(55.0)	88%
Property Taxes	25.1	25.1	-	100%
Power Sales	3.5	4.2	0.7	120%
Interest Income	3.3	3.3	-	100%
SCC Revenues	26.0	26.0	-	100%
Reimbursements	11.2	11.2	-	100%
All Other Revenue	17.4	17.4	-	100%
Drought Surcharge / Excessive Use		5.0	5.0	
TOTAL REVENUES	539.5	490.2	(49.3)	91%
Operating Expenses:				
Operations	262.2	244.6	17.6	93%
Debt Service	180.2	177.6	2.6	99%
Drought Expenses ¹		0.0	-	N/A
TOTAL OPERATING EXPENSES	442.4	422.2	20.2	95%

NET VARIANCE COMPARED TO BUDGET	(29.1)	-
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¹ Drought contingency appropriation of \$62.1 million not shown above.

Revenues

FY17 total revenues are projected to be \$490.2 million or 91 percent of budget. Water charges revenue is projected to be \$55.0 million less than budget due to anticipated customer conservation which historically follows a period of drought. Again, the budget assumed 151 MGD, while average year-end water sales projections for FY17 are based on 129 MGD equal to the FY16 consumption level. The projected drought surcharge revenue would be incurred in FY16, but would be received in FY17 due to the billing cycle.

No additional drought-related revenues are anticipated in FY17 other than the FY16 drought revenue mentioned above.

Expenses

Total FY17 operating expenses are projected to be \$20.2 million less than budget. Budget savings are primarily driven by unspent contingency, higher than budgeted operating reimbursements for the administration of capital projects, slightly lower debt service expenses, and other operation expense savings.

No drought expenses are anticipated in FY17 other than the potential final payments associated with the FY16 supplemental water purchases. At the time of this report, it is uncertain whether there will be final FY16 supplemental water payments; the projected payments are anticipated to be less than \$5 million.

Net Budget Variance

Despite the normal operations expense saving offset, the Water System is projected to end FY17 with an unfavorable net budget variance of \$29.1 million. Rate stabilization funds will be used to maintain the District's policy level for debt coverage of 1.6.

Capital Budget

The Board approved the Water System FY16 through FY20 Capital Improvement Program (CIP) and adopted capital appropriations for the first two years of the CIP. Adopted appropriations are used to fund expenditures over a multi-year period for each capital project, while cash flows reflect the amount estimated to be spent in a given year. Water System rates are set based on estimated cash flow expenditures.

The FY16 capital budget included \$249.0 million in appropriations with a planned cash flow expenditure of \$224.5 million. Projected FY16 capital cash flow expenditures are estimated to be \$207.0 million or 93 percent of the planned cash flow due to delays in the Raw Water Infrastructure, Reservoir Rehabilitation and Dam Seismic Upgrades projects.

There are no recommended revisions to the FY17 adopted appropriation of \$290.4 million, or the planned cash flow of \$236.1 million which is sufficient to meet CIP funding needs.

Fiscal Year 2017 Staffing Changes

The FY17 budget authorized the addition of three positions in the Water System: one regular position to support technology infrastructure and cyber-security; and two limited-term (LT) positions to support advanced drought-related actions. The two drought-related positions are not expected to be filled.

Staff is proposing the addition of one temporary construction (TC) Construction Inspector position for a developer-funded pipeline project. The cost of this staffing change can be managed within the existing budget as the District will be reimbursed by the developer.

ENGINEERING DEPARTMENT						
FY	Action	From Classification(s)	To Classification(s)	Change in Cost	Change in FTE	Project/Program
2017	Add Position		Construction Inspector	\$ 172,543	1.0	Faria Pipeline Project

Bargaining Unit Changes

The following table shows the net change in bargaining unit status from the adopted FY16 budget and the addition of the proposed position in Engineering.

FY17 vs. FY16 Net Change in Bargaining Unit Status							
Department	Local 2019	Local 444	Local 21	Local 39	MGMT / Confi- dential	Non- Rep	Civil Service Exempt
Operations & Maintenance Support							
Maintenance & Construction	1						
Water Operations							
Water Resources							
Natural Resources							
Engineering & Construction ¹	1						
Office of the General Manager							
Finance							
Information Systems							
Customer & Community Services ²	2						
Human Resources							
Office of the General Counsel							
Water Recycling Program							
Administration							
Total Net Change	4	0	0	0	0	0	0

¹ District reimbursed by developer for proposed new position

² New drought positions not anticipated to be filled

WASTEWATER SYSTEM

Fiscal Year 2016

Summary

The Wastewater System is projected to end FY16 with a favorable net budget variance of \$6.3 million. Revenues are projected to be \$3.5 million greater than budget, and operating expenses are projected to be \$2.8 million less than budget.

The following table presents the FY16 Wastewater System revenue and operating expense projection compared to budget, followed by a description of the key budget drivers.

FY16 Wastewater System Revenue and Expense Summary (\$Millions)	Amended Budget	Year-end Projection	Variance Favorable / (Unfavorable)	% of Budget
Operating Revenues:				
Treatment Charges	66.9	64.9	(2.0)	97%
Resource Recovery	8.0	11.6	3.6	145%
Wet Weather Facilities Charge	21.8	21.8	-	100%
Property Taxes	4.3	4.3	-	100%
Ad Valorem Bond Levy	4.0	4.0	-	100%
Interest Income	0.4	0.3	(0.1)	75%
Laboratory Services	3.9	4.2	0.3	108%
Reimbursements	1.0	1.8	0.8	180%
Permit Fees	1.8	1.7	(0.1)	94%
Capacity Charges	1.5	2.6	1.1	173%
All Other Revenue	5.7	5.6	(0.1)	98%
Total Revenues	119.3	122.8	3.5	103%
Operating Expenses:				
Operations	65.4	62.7	2.7	96%
Debt Service	33.7	33.6	0.1	100%
TOTAL OPERATING EXPENSES	99.1	96.3	2.8	97%
NET VARIANCE COMPARED TO BUDGET			6.3	-

Revenues

Total FY16 revenues are projected to be \$122.8 million or 103 percent of budget. Treatment charges are projected to be \$2.0 million less than budget as a result of customer conservation, but the shortfall is offset by above budget revenues for Resource Recovery of \$3.6 million, Capacity Charges of \$1.1 million, and reimbursements of \$0.8 million.

Expenses

FY16 total operating expenses are projected to be \$2.8 million less than budget. Budget savings are driven by unspent contingency, higher than budgeted operating reimbursements for the administration of capital projects, and other operation expense savings.

Net Budget Variance

The Wastewater System is projected to end FY16 with a favorable net budget variance of \$6.3 million.

Fiscal Year 2017

Summary

The Wastewater System is projected to end FY17 with a favorable net budget variance of \$3.2 million. Revenues are projected to be at budget, and operating expenses are projected to be \$3.2 million less than budget.

The following table presents the FY17 Wastewater System revenue and operating expense projection compared to budget, followed by a description of the key budget drivers.

FY17 Wastewater System Revenue and Expense Summary (\$Millions)	Adopted Budget	Year-end Projection	Variance Favorable / (Unfavorable)	% of Budget
Operating Revenues:				
Treatment Charges	70.3	68.3	(2.0)	97%
Resource Recovery	8.0	10.0	2.0	125%
Wet Weather Facilities Charge	22.9	22.9	-	100%
Property Taxes	4.4	4.4	-	100%
Ad Valorem Bond Levy	4.1	4.1	-	100%
Interest Income	0.7	0.7	-	100%
Laboratory Services	4.0	4.0	-	100%
Reimbursements	1.0	1.0	-	100%
Permit Fees	1.8	1.8	-	100%
Capacity Charges	1.6	1.6	-	100%
All Other Revenue	5.7	5.7	-	100%
Total Revenues	124.5	124.5	-	100%
Operating Expenses:				
Operations	70.7	67.6	3.1	96%
Debt Service	34.0	33.9	0.1	100%
TOTAL OPERATING EXPENSES	104.7	101.5	3.2	97%
NET VARIANCE COMPARED TO BUDGET			3.2	-

Revenues

FY17 total revenues are projected to be \$124.5 million or 100 percent of budget. Treatment charges are projected to be \$2.0 million less than budget as a result of continued customer conservation, but this shortfall is offset by a projected \$2.0 million higher than budgeted in Resource Recovery revenue.

Expenses

Total FY17 operating expenses are projected to be \$3.2 million less than budget. Budget savings are primarily driven by unspent contingency and other operation expense savings.

Net Budget Variance

The Wastewater System is projected to end FY17 with a favorable net budget variance of \$3.2 million.

Capital Budget

The Board approved the Wastewater System FY16 through FY20 Capital Improvement Program (CIP) and adopted capital appropriations for the first two years of the CIP. Adopted appropriations are used to fund expenditures over a multi-year period for each capital project, while cash flows reflect the amount estimated to be spent in a given year. Wastewater System rates are based on estimated planned cash flows.

The FY16 capital budget included \$70.5 million in appropriations with a planned cash flow expenditure of \$39.0 million. Projected FY16 capital cash flow expenditures are estimated to be \$36.4 million or 94 percent of the planned cash flow due to delays in the Digester Upgrade and Treatment Plant Infrastructure projects.

There are no recommended revisions to the FY17 approved capital appropriation of \$32.6 million, or the planned cash flow of \$36.7 million which is sufficient to meet CIP funding needs.

Fiscal Year 2017 Staffing Changes

There are no FY17 staffing changes for the Wastewater System.